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IN THE

Supreme Court of the United States

OCTOBER TERM, 1961.

No. 447.

ESTATE OF THALIA E. GRAFF SMITH, DECEASED, SYLVESTER C. SMITH, JR., EXECUTOR, and SYLVESTER C. SMITH, JR.,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

MARK G. ANTON and ADELE B. ANTON,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT.

REPLY BRIEF FOR PETITIONERS.

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The basic purpose of this Reply is to question the Commissioner's endeavor to distinguish deficiency dividends from other dividends. In the humble opinion of the Petitioners, the fact that the shareholders availed themselves

of a procedure to their tax advantage, in no way makes deficiency dividends any different than other dividends.

In opposing the Petition for the Writ of Certiorari, the Commissioner states:

> "If the Court, however, construes the opinion to mislead the tax bar by necessarily establishing a general rule inconsistent with Treasury policy and the government's reading of the law, the proper course would be to grant certiorari and either affirm the decision after argument upon the narrower ground or remand the case now for consideration of that ground in the court of appeals." (R. B. in O. p. 6).

The Commissioner also states that:

> "* * * if the decision below necessarily held that all original owners are taxable as a general rule and no special circumstances were present—we would agree that the writ should be granted." (R. B. in O. p. 4).

Petitioners respectfully urge that only such general question was determined and no justifiable ground exists for any narrower construction. The Third Circuit Court of Appeals makes no distinction whatsoever between deficiency dividends and other dividends, and none is warranted.

Deficiency dividends are treated as normal dividends with respect to the incidents of taxation in the hands of the recipient. Neither the Internal Revenue Code, nor the Regulations promulgated thereunder, changes the general rule of dividend taxation where deficiency dividends are concerned. For the Commissioner to assert otherwise is to

do so without legal support. Section 39.506-4 of Regulations 118, states with respect to deficiency dividends:

> "'The deficiency dividends' are required under Section 506 (c) to be paid prior to the filing of the claim for credit or refund and such dividends must be of such a nature as to constitute taxable dividends in the hands of such of the shareholders as are subject to taxation under Chapter I for the year in which paid (see section 27 (i)) and must be non-preferential (see section 27 (h))."

Particular notice must be taken of the words, "such shareholders as are subject to taxation under Chapter I for the year in which paid. * * *" The donees of the stock and the recipients of the dividends, the c. ldren, fully satisfy the definition of "shareholders subject to taxation under Chapter I for the year in which paid."

The Regulations charge the owner of the stock with the dividend for the year in which such dividend is paid. Nowhere in the Internal Revenue Code, the Regulations, nor in the case law, is there any requirement that the stockholders chargeable with dividend income, must be stockholders of the corporation at the time that the profits or income, from which the dividends are derived, be earned by the corporation. The stockholders need merely be the owners of the stock on the record date when the dividend is paid. Deficiency dividends, like all dividends, are charged to the owner of the stock for the year in which such dividends are paid.

It is humbly submitted that the dividends paid to the donees of the stock in the instant case, fully satisfy the requirements under Section 39.506-4 (3) of Regulations 118.

They were non-preferential and were fully taxable, and so reported by the shareholders for the period in which the distribution was made, as required by section 27 (h) and 27 (i), respectively, under the 1939 Internal Revenue Code.

The Commissioner's contention that different treatment be accorded deficiency dividends, constitutes an attempt to legislate, a function clearly not a matter for disposition by this Honorable Court.

Wherefore, it is respectfully prayed that the Petition for a Writ of Certiorari be granted.

Respectfully submitted,

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Counsel for Petitioners.

Dated: January 2, 1962.